

## The Spending Outlook

The Congressional Budget Office expects that federal spending in 2004 will continue to grow at a significant rate but less rapidly than in 2003. Under the assumptions that current laws for mandatory programs remain the same and that discretionary appropriations total about \$876 billion, CBO estimates that outlays in 2004 will rise by \$137 billion, to \$2.3 trillion—a 6.3 percent increase over their level in 2003 (see *Tables 3-1 and 3-2 on pages 50 and 51*). Total spending, excluding net interest, is estimated to rise by 6.7 percent in 2004, compared with an increase of 8.9 percent in 2003.

Fueling the growth in outlays in 2004 are increases in discretionary spending (a portion of which comes from budget authority granted before 2004) and continued growth in entitlement programs. In addition, CBO estimates that net interest payments will rise by 2 percent in 2004, their first increase since 1997. Outlays for defense discretionary programs are estimated to climb by \$46 billion (11.5 percent) in 2004; for nondefense discretionary programs, the expected increase is \$24 billion (5.8 percent). Spending for entitlements and other mandatory programs—which constitutes more than half of all federal spending—is estimated to grow by \$63 billion (5.3 percent) over its level in 2003 (see *Box 3-1* for descriptions of the various types of federal spending).

Total spending as a percentage of gross domestic product fell from a peak of 23.5 percent in 1983 to a low of 18.4 percent in 2000. However, increases in spending and lagging economic growth pushed that figure up to 18.6 percent in 2001, 19.4 percent in 2002, and 19.9 percent in 2003. CBO estimates that outlays will reach 20.0 percent of GDP in 2004 and under current policies will remain at about that level from 2005 through 2014 (the 10-year projection period).

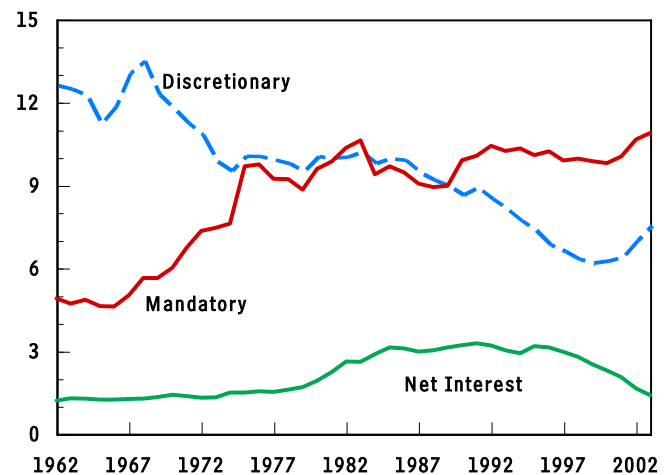
The mix of federal spending has changed significantly over the past several decades. Today, the government spends less—as a proportion of GDP—on discretionary activities and more on entitlement programs than it did in the past. Discretionary spending has declined from 12.7 percent of GDP in 1962 to 7.6 percent in 2003 (see *Figure 3-1*). In contrast, spending for entitlements and other mandatory programs (net of offsetting receipts) has climbed from 4.9 percent to 10.9 percent of GDP over the same period. (For detailed annual data on spending since 1962, see *Appendix F*.)

In 2004, discretionary spending is expected to grow as a percentage of GDP from 7.6 percent to 7.8 percent,

**Figure 3-1.**

### Major Components of Spending, 1962 to 2003

(Percentage of GDP)



Source: Congressional Budget Office based on data from the Office of Management and Budget.

**Box 3-1.****Categories of Federal Spending**

Federal spending can be divided into categories on the basis of its treatment in the budget process:

**Discretionary spending** pays for activities such as defense, transportation, national parks, and foreign aid. Discretionary programs are controlled by annual appropriation acts; policymakers decide each year how many dollars to devote to which activities. Certain fees and other charges that are triggered by appropriation action are classified as offsetting collections, which offset discretionary spending. The Congressional Budget Office's (CBO's) baseline depicts the path of discretionary spending in accordance with provisions of the Balanced Budget and Emergency Deficit Control Act of 1985, which state that current spending should be assumed to grow with inflation in the future.<sup>1</sup> CBO estimates that appropriations provided for this fiscal year total \$460 billion for defense and about \$416 billion for nondefense activities. In addition to the \$876 billion in budget authority for discretionary programs for 2004, the baseline reflects about \$43 billion in obligation limitations that control spending from the Highway Trust Fund and the Airport and Airway Trust Fund. Such spending is classified as discretionary; however, the budget authority for such pro-

grams is provided in authorizing legislation and is not considered discretionary.

**Mandatory spending** consists overwhelmingly of benefit programs such as Social Security, Medicare, and Medicaid. The Congress generally determines spending for those programs by setting rules for eligibility, benefit formulas, and other parameters rather than by appropriating specific dollar amounts each year. CBO's baseline projections of mandatory spending assume that existing laws and policies remain unchanged and that most expiring programs will be extended. Mandatory spending also includes offsetting receipts—fees and other charges that are recorded as negative budget authority and outlays. Offsetting receipts differ from revenues in that revenues generally are collected as an exercise of the government's sovereign powers, whereas most offsetting receipts are collected from other government accounts or paid by the public for businesslike transactions (such as rents and royalties from leases for oil and gas drilling on the Outer Continental Shelf).

**Net interest** includes interest paid on Treasury securities and other interest that the government pays (for example, on late refunds issued by the Internal Revenue Service) minus interest that the government collects from various sources (such as from commercial banks, where Treasury tax and loan accounts are maintained). Net interest is determined by the size and composition of the government's debt, annual budget deficits or surpluses, and market interest rates.

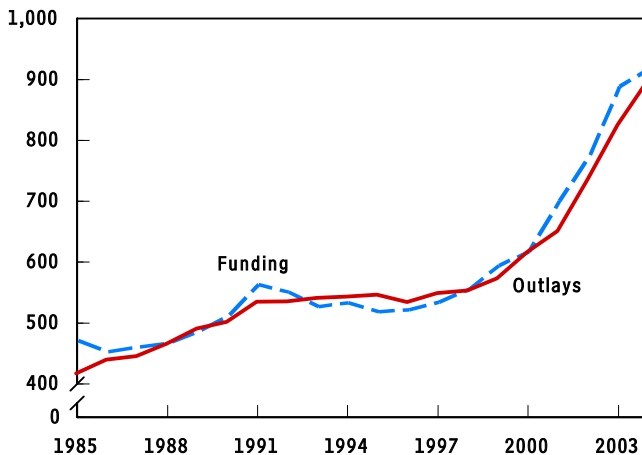
1. The inflation rates used in CBO's baseline, as specified by the Deficit Control Act, are the employment cost index for wages and salaries (applied to expenditures related to federal personnel) and the GDP deflator (for other expenditures).

mandatory spending is expected to drop slightly to 10.8 percent (from 10.9 percent in 2003), and net interest is expected to remain at 1.4 percent. After 2004, under assumptions required by law for the baseline, discretionary outlays are projected to grow roughly half as fast as the economy, or at an average annual rate of 2.5 percent. As a result, discretionary spending's share of GDP is projected

to decline gradually, reaching 6.4 percent in 2014. For mandatory spending, the outlook differs. Led by growth in the two major health care programs, Medicare and Medicaid, mandatory outlays (net of offsetting receipts) will grow slightly faster than the economy—or at a rate of 5.5 percent—if current policies remain unchanged. At that rate, those outlays will claim 11.8 percent of GDP

**Figure 3-2.****Discretionary Funding and Outlays, 1985 to 2004**

(Billions of dollars)



Source: Congressional Budget Office.

Note: Discretionary funding includes both budget authority and obligation limitations. (Spending from the Highway Trust Fund and the Airport and Airway Trust Fund is subject to such limitations. Budget authority for those programs is provided in authorizing legislation and is not considered discretionary.)

by 2014—about a percentage point above their current share. CBO projects that interest payments as a percentage of GDP will increase by one-third—growing to 2.1 percent of GDP in 2009 as a result of continuing deficits and the rising interest rates in CBO’s economic forecast (see Chapter 2 for details of CBO’s economic outlook). That percentage will fall slightly toward the end of the 10-year period as the baseline assumptions of restrained growth in discretionary outlays and the scheduled expiration of the tax provisions in the Economic Growth and Tax Relief Reconciliation Act of 2001 lead to diminished borrowing.

## Discretionary Spending

Each year, the Congress starts the appropriation process anew. The annual appropriation acts that it passes provide new budget authority (the authority to enter into financial obligations) for discretionary programs and activities. That authority translates into outlays when the money is actually spent. Although some funds (for example, those for employees’ salaries) are spent quickly, others (for example, for major construction projects) are dis-

bursed over several years. In any given year, discretionary outlays include spending from both new budget authority and from amounts appropriated previously.

### Recent Trends in Discretionary Funding and Outlays

Total discretionary outlays as a share of GDP have been climbing steadily since 2001. That recent upswing reverses a downward trend since the mid-1980s. At that time, discretionary outlays accounted for 10.0 percent of GDP, but they fell to 6.3 percent in 1999 and 2000. Since then, such outlays have moved upward, and they are estimated to account for 7.8 percent of GDP in 2004 (see Table 3-3 on page 52).

Defense outlays declined sharply as a share of the economy during the late 1980s and 1990s, decreasing from a peak of 6.2 percent in 1986 to a low of 3.0 percent in 1999, 2000, and 2001. Those outlays then began to rise, reaching 3.4 percent of GDP in 2002 and 3.7 percent of GDP in 2003, an increase in nominal dollar terms of more than one-third from 2000 to 2003. Defense outlays will grow by another 11.5 percent to reach 3.9 percent of GDP this year, CBO estimates, assuming no additional funding for military activity in Iraq and Afghanistan or other defense needs in 2004.

Nondefense discretionary spending has remained relatively constant as a share of GDP since the mid-1980s (hovering between 3.2 percent and 3.9 percent of GDP), although it has grown in nominal dollar terms; such spending is estimated to total 3.9 percent of GDP in 2004. The growth rate of nondefense outlays has slowed significantly since 2002, dropping from 12.3 percent in that year to an estimated 5.8 percent in 2004.

The growth of outlays reflects sizable increases in discretionary funding (which comprises budget authority and obligation limitations) over the past four years (see Figure 3-2).<sup>1</sup> Some of the recent increases in funding are attributable to supplemental appropriations for recovery from and response to the terrorist attacks of September 11, 2001; the wars in Afghanistan and Iraq; and disaster

1. In addition to the \$876 billion in budget authority for discretionary programs in 2004, the baseline reflects about \$43 billion in obligation limitations that control spending from the Highway Trust Fund and the Airport and Airway Trust Fund. Such spending is classified as discretionary; however, the budget authority for such programs is provided in authorizing legislation and is not considered discretionary.

**Table 3-1.****CBO's Projections of Spending Under Its Baseline**

	Actual												Total, 2005- 2009	Total, 2005- 2014
	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014		
In Billions of Dollars														
Outlays														
Discretionary Spending														
Defense	405	451	470	476	482	498	510	523	541	545	564	579	2,437	5,189
Nondefense	421	445	466	478	490	500	510	522	533	545	558	571	2,445	5,174
Subtotal	826	896	936	955	972	998	1,021	1,045	1,075	1,091	1,122	1,149	4,882	10,363
Mandatory Spending														
Social Security	471	492	513	533	559	587	618	653	690	732	778	827	2,809	6,490
Medicare	274	294	317	369	418	448	478	515	557	592	645	698	2,029	5,035
Medicaid	161	174	179	186	195	212	230	250	271	295	320	348	1,003	2,487
Other <sup>a</sup>	273	281	287	262	252	258	265	269	277	253	257	256	1,323	2,635
Subtotal	1,179	1,242	1,295	1,350	1,424	1,504	1,591	1,687	1,796	1,872	2,000	2,129	7,165	16,647
Net Interest	153	156	180	219	255	281	300	316	328	334	335	338	1,235	2,886
<b>Total</b>	<b>2,158</b>	<b>2,294</b>	<b>2,411</b>	<b>2,525</b>	<b>2,652</b>	<b>2,783</b>	<b>2,912</b>	<b>3,047</b>	<b>3,198</b>	<b>3,296</b>	<b>3,457</b>	<b>3,616</b>	<b>13,282</b>	<b>29,897</b>
On-budget	1,795	1,904	2,012	2,118	2,233	2,350	2,461	2,575	2,704	2,785	2,914	3,048	11,175	25,201
Off-budget	363	391	399	406	419	433	451	472	494	512	543	568	2,107	4,696
As a Percentage of GDP														
Outlays														
Discretionary Spending														
Defense	3.7	3.9	3.9	3.8	3.6	3.6	3.5	3.4	3.4	3.3	3.3	3.2	3.7	3.5
Nondefense	3.9	3.9	3.9	3.8	3.7	3.6	3.5	3.4	3.4	3.3	3.2	3.2	3.7	3.5
Subtotal	7.6	7.8	7.7	7.5	7.3	7.2	7.0	6.9	6.8	6.6	6.5	6.4	7.4	6.9
Mandatory Spending														
Social Security	4.3	4.3	4.2	4.2	4.2	4.2	4.3	4.3	4.4	4.4	4.5	4.6	4.2	4.3
Medicare	2.5	2.6	2.6	2.9	3.2	3.2	3.3	3.4	3.5	3.6	3.7	3.9	3.1	3.4
Medicaid	1.5	1.5	1.5	1.5	1.5	1.5	1.6	1.6	1.7	1.8	1.8	1.9	1.5	1.7
Other <sup>a</sup>	2.5	2.5	2.4	2.1	1.9	1.9	1.8	1.8	1.7	1.5	1.5	1.4	2.0	1.8
Subtotal	10.9	10.8	10.7	10.6	10.8	10.9	11.0	11.1	11.3	11.3	11.6	11.8	10.8	11.1
Net Interest	1.4	1.4	1.5	1.7	1.9	2.0	2.1	2.1	2.1	2.0	1.9	1.9	1.9	1.9
<b>Total</b>	<b>19.9</b>	<b>20.0</b>	<b>19.9</b>	<b>19.9</b>	<b>20.0</b>	<b>20.1</b>	<b>20.1</b>	<b>20.1</b>	<b>20.2</b>	<b>19.9</b>	<b>20.0</b>	<b>20.0</b>	<b>20.0</b>	<b>20.0</b>
On-budget	16.6	16.6	16.6	16.7	16.9	17.0	17.0	17.0	17.0	16.8	16.8	16.9	16.8	16.9
Off-budget	3.4	3.4	3.3	3.2	3.2	3.1	3.1	3.1	3.1	3.1	3.1	3.1	3.2	3.1
Memorandum:														
Gross Domestic Product														
(Billions of dollars)	10,829	11,469	12,091	12,682	13,236	13,862	14,519	15,187	15,862	16,562	17,301	18,070	66,389	149,371

Source: Congressional Budget Office.

a. Includes offsetting receipts.

**Table 3-2.****Average Annual Rates of Growth in Outlays Under CBO's Baseline**

(Percent)

	Actual 1992-2002	Actual 2002-2003	Estimated 2003-2004	Projected <sup>a</sup> 2004-2014
Discretionary	3.2	12.4	8.6	2.5
Defense	1.4	16.0	11.5	2.5
Nondefense	5.2	9.2	5.8	2.5
Mandatory	5.5	6.6	5.3	5.5
Social Security	4.7	4.1	4.6	5.3
Medicare	7.0	8.1	7.3	9.0
Medicaid	8.1	8.9	8.4	7.2
Other <sup>b</sup>	4.3	8.4	2.7	-0.9
Net Interest	-1.5	-10.5	2.0	8.0
Total Outlays	3.8	7.3	6.3	4.7
Total Outlays Excluding Net Interest	4.5	8.9	6.7	4.4
<b>Memorandum:</b>				
Consumer Price Index	2.5	2.3	1.7	2.1
Nominal GDP	5.2	4.4	5.9	4.7
Discretionary Funding <sup>c</sup>	3.4	14.8	3.2	2.4
Defense	1.9	26.1	1.1	2.4
Nondefense	5.0	5.0	5.3	2.4

Source: Congressional Budget Office.

- a. As specified by the Deficit Control Act, CBO's baseline uses the employment cost index for wages and salaries to inflate discretionary spending related to federal personnel and the GDP deflator to adjust other spending.
- b. Includes offsetting receipts.
- c. Comprises budget authority and obligation limitations.

relief. Such appropriations—combined with funding increases for other activities—contributed to annual growth rates for discretionary funding of between 10 percent and 15 percent from 2001 through 2003. Funding thus far for 2004 (including the omnibus appropriation act) represents an increase of 3.2 percent from last year's level—1.1 percent for defense and 5.3 percent for nondefense activities. That increase in nondefense funding stems in large part from spending for the reconstruction of Iraq. Within the nondefense category, funding for homeland security for 2004 is slightly less than it was in 2003, because the 2003 funding included certain one-time costs of the Transportation Security Administration.

**Discretionary Spending for 2005 Through 2014**

Under baseline assumptions, CBO projects that discretionary outlays will continue rising and remain about

evenly divided between defense and nondefense activities for the 2005-2014 period.<sup>2</sup> Outlays for each category of discretionary spending are projected to total about \$470 billion in 2005 and to grow by more than \$100 billion by 2014.

**Homeland Security.** An area of spending that includes both defense and nondefense activities is homeland security. The Administration has identified the spending that it considers related to such activities, and in its current baseline, CBO has adopted the Administration's classifi-

2. Most spending for defense programs is classified as discretionary; an additional \$2 billion to \$4 billion a year in defense spending is classified as mandatory.

**Table 3-3.****Defense and Nondefense Discretionary Outlays**

	Defense Outlays			Nondefense Outlays			Total Discretionary Outlays		
	In Billions of Dollars	As a Percentage of GDP	Percentage Change from Previous Year	In Billions of Dollars	As a Percentage of GDP	Percentage Change from Previous Year	In Billions of Dollars	As a Percentage of GDP	Percentage Change from Previous Year
1985	253	6.1	11.0	163	3.9	7.5	416	10.0	9.6
1986	274	6.2	8.2	165	3.7	1.2	439	10.0	5.5
1987	283	6.1	3.2	162	3.5	-1.8	444	9.5	1.3
1988	291	5.8	3.0	174	3.5	7.3	464	9.3	4.6
1989	304	5.6	4.5	185	3.4	6.5	489	9.0	5.2
1990	300	5.2	-1.3	200	3.5	8.5	501	8.7	2.4
1991	320	5.4	6.5	214	3.6	6.6	533	9.0	6.5
1992	303	4.9	-5.3	231	3.7	8.2	534	8.6	0.1
1993	292	4.5	-3.4	247	3.8	6.8	539	8.2	1.0
1994	282	4.1	-3.5	259	3.7	4.9	541	7.8	0.4
1995	274	3.7	-3.1	271	3.7	4.7	545	7.4	0.6
1996	266	3.5	-2.8	267	3.5	-1.7	533	6.9	-2.2
1997	272	3.3	2.1	276	3.4	3.3	547	6.7	2.7
1998	270	3.1	-0.5	282	3.2	2.3	552	6.4	0.9
1999	275	3.0	1.9	297	3.2	5.2	572	6.3	3.6
2000	295	3.0	7.1	320	3.3	7.9	615	6.3	7.5
2001	306	3.0	3.8	343	3.4	7.3	649	6.5	5.6
2002	349	3.4	14.0	385	3.7	12.3	734	7.1	13.1
2003	405	3.7	16.0	421	3.9	9.2	826	7.6	12.4
2004 <sup>a</sup>	451	3.9	11.5	445	3.9	5.8	896	7.8	8.6

Sources: Office of Management and Budget for 1985 through 2003 and Congressional Budget Office for 2004.

a. Estimated.

cation.<sup>3</sup> (See *Appendix C* for more details on homeland security and trends in spending for that purpose.) Net discretionary budget authority for homeland security is estimated to total about \$37 billion in 2004—\$11 billion for defense and \$26 billion for nondefense programs. CBO estimates that the resulting discretionary outlays for those activities will total \$33 billion this year (see

*Table 3-4*). In addition, roughly \$1 billion a year in net outlays for homeland security is classified as mandatory spending. Under its baseline assumptions, CBO projects that discretionary outlays for homeland security will average about 0.3 percent of GDP and about 1.4 percent of total federal spending over the next 10 years.

**Alternative Paths for Discretionary Spending.** As specified in the Deficit Control Act, CBO inflates discretionary budget authority (using the factors set forth in law) from the level appropriated in the current year to provide a reference point for assessing policy changes. CBO's baseline assumes that total budget authority for 2004 is about \$876 billion and obligation limitations total \$43 billion; both grow with inflation thereafter. Under those assumptions, discretionary funding would grow at an annual rate of about 2.5 percent for most of the projection

3. CBO received some preliminary information from the Administration regarding the classification of appropriations for 2004 as homeland security spending. For certain accounts, however, CBO estimated the homeland security spending for 2004 on the basis of the amounts designated for that activity in the President's budget for 2004. Once the Administration releases its 2005 budget proposal in February 2004, CBO will review its homeland security estimates to reflect the Administration's actual classification of those programs.

**Table 3-4.****CBO's Baseline Projections of Discretionary Spending for Homeland Security**

(Billions of dollars)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Total, 2005- 2009	Total, 2005- 2014
Budget Authority													
Defense	11	11	11	11	12	12	12	13	13	13	14	57	121
Nondefense <sup>a</sup>	26	29	27	27	28	31	29	30	31	32	33	141	297
<b>Total</b>	<b>37</b>	<b>39</b>	<b>38</b>	<b>39</b>	<b>39</b>	<b>43</b>	<b>42</b>	<b>43</b>	<b>44</b>	<b>45</b>	<b>46</b>	<b>198</b>	<b>418</b>
Outlays (Net)													
Defense	10	11	11	11	11	12	12	12	13	13	13	56	119
Nondefense	23	25	27	28	29	29	30	31	31	32	33	139	295
<b>Total</b>	<b>33</b>	<b>36</b>	<b>38</b>	<b>40</b>	<b>40</b>	<b>41</b>	<b>42</b>	<b>43</b>	<b>44</b>	<b>45</b>	<b>46</b>	<b>194</b>	<b>414</b>
<b>Memorandum:</b>													
Net Mandatory Outlays for Homeland Security	1	1	1	1	1	1	1	1	1	1	1	6	12

Source: Congressional Budget Office.

Notes: CBO's classification of homeland security funding is based on designations established by the Administration. Those designations are not limited to the activities of the Department of Homeland Security. In fact, some activities of the department, such as disaster relief, are not included in the definition, whereas nondepartmental activities (such as some defense-related programs and some funding for the National Institutes of Health) fall within the Administration's definition of homeland security. About half of all spending considered to be for homeland security is for activities outside of the Department of Homeland Security. (*See Appendix C.*)

CBO received some preliminary information from the Administration regarding the classification of appropriations for 2004 as homeland security spending. For certain accounts, however, CBO estimated the homeland security spending for 2004 on the basis of the amounts designated for such activity in the President's budget for 2004. When the Administration releases its budget in February 2004, CBO will review its homeland security estimates to reflect the Administration's actual classification of those programs.

The amounts shown in this table reflect the net spending for homeland security activities. About \$3 billion to \$4 billion a year in spending is offset by fees and other receipts, mostly in the discretionary category.

- a. Project BioShield, an initiative to expand the government's arsenal of counter-bioterrorism agents, has appropriations for 2004, 2005, and 2009 in CBO's baseline. Budget authority for all other years is zero.

period. Because actual policies can and probably will differ from those assumptions, CBO presents alternative paths for discretionary spending to show the budgetary consequences of different rates of growth (*see Table 3-5*).

The first alternative path assumes that discretionary funding increases by 6.9 percent each year after 2004. That rate of growth is the historical average from 1999 through 2004, excluding the \$87 billion in supplemental appropriations enacted in November 2003. As the base-

line does, however, this path includes those supplemental appropriations in total budget authority for 2004 and extends them through 2014. If discretionary funding increased at that historical rate of growth, discretionary outlays over the 10-year period would total \$2.7 trillion more than the baseline figures presented in this report, and debt-service costs would increase by nearly \$0.5 trillion.

**Table 3-5.****CBO's Projections of Discretionary Spending Under Alternative Paths**

(Billions of dollars)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Total, 2005- 2009	Total, 2005- 2014
<b>Baseline (Discretionary Funding Grows with Inflation After 2004)<sup>a</sup></b>													
Budget Authority													
Defense	460	473	481	492	504	517	530	543	557	571	586	2,468	5,255
Nondefense	416	431	436	446	457	470	480	491	503	516	529	2,241	4,760
<b>Total</b>	<b>876</b>	<b>904</b>	<b>918</b>	<b>939</b>	<b>961</b>	<b>988</b>	<b>1,010</b>	<b>1,035</b>	<b>1,060</b>	<b>1,087</b>	<b>1,115</b>	<b>4,709</b>	<b>10,015</b>
Outlays													
Defense	451	470	476	482	498	510	523	541	545	564	579	2,437	5,189
Nondefense	445	466	478	490	500	510	522	533	545	558	571	2,445	5,174
<b>Total</b>	<b>896</b>	<b>936</b>	<b>955</b>	<b>972</b>	<b>998</b>	<b>1,021</b>	<b>1,045</b>	<b>1,075</b>	<b>1,091</b>	<b>1,122</b>	<b>1,149</b>	<b>4,882</b>	<b>10,363</b>
<b>Discretionary Funding Grows by 6.9 Percent a Year After 2004<sup>b</sup></b>													
Budget Authority													
Defense	460	496	530	566	605	647	692	739	791	846	904	2,843	6,815
Nondefense	416	452	482	517	553	595	635	680	728	779	835	2,599	6,255
<b>Total</b>	<b>876</b>	<b>948</b>	<b>1,012</b>	<b>1,083</b>	<b>1,158</b>	<b>1,242</b>	<b>1,326</b>	<b>1,419</b>	<b>1,518</b>	<b>1,625</b>	<b>1,739</b>	<b>5,442</b>	<b>13,070</b>
Outlays													
Defense	451	484	513	544	585	626	669	720	760	818	875	2,752	6,593
Nondefense	445	477	509	543	577	615	655	697	743	792	845	2,720	6,453
<b>Total</b>	<b>896</b>	<b>961</b>	<b>1,022</b>	<b>1,087</b>	<b>1,162</b>	<b>1,240</b>	<b>1,323</b>	<b>1,417</b>	<b>1,503</b>	<b>1,610</b>	<b>1,720</b>	<b>5,472</b>	<b>13,046</b>
<b>Discretionary Funding Grows at the Rate of Nominal GDP After 2004</b>													
Budget Authority													
Defense	460	489	512	535	560	586	613	640	669	699	730	2,682	6,034
Nondefense	416	446	466	487	510	537	560	585	612	640	669	2,447	5,513
<b>Total</b>	<b>876</b>	<b>935</b>	<b>978</b>	<b>1,022</b>	<b>1,070</b>	<b>1,124</b>	<b>1,173</b>	<b>1,226</b>	<b>1,281</b>	<b>1,339</b>	<b>1,399</b>	<b>5,129</b>	<b>11,547</b>
Outlays													
Defense	451	480	500	519	547	573	599	631	649	684	714	2,619	5,897
Nondefense	445	474	498	522	544	568	592	617	643	670	699	2,606	5,826
<b>Total</b>	<b>896</b>	<b>954</b>	<b>999</b>	<b>1,041</b>	<b>1,091</b>	<b>1,140</b>	<b>1,191</b>	<b>1,248</b>	<b>1,292</b>	<b>1,354</b>	<b>1,413</b>	<b>5,224</b>	<b>11,723</b>
<b>Discretionary Funding, Excluding Supplemental Appropriations, Grows with Inflation After 2004</b>													
Budget Authority													
Defense	460	406	414	423	434	445	456	468	480	492	505	2,123	4,524
Nondefense	416	409	414	423	433	446	455	466	478	490	502	2,125	4,516
<b>Total</b>	<b>876</b>	<b>815</b>	<b>827</b>	<b>847</b>	<b>867</b>	<b>891</b>	<b>911</b>	<b>934</b>	<b>958</b>	<b>982</b>	<b>1,007</b>	<b>4,248</b>	<b>9,041</b>
Outlays													
Defense	451	436	418	417	429	440	451	466	470	486	499	2,141	4,513
Nondefense	445	460	464	471	478	488	499	510	521	533	545	2,362	4,970
<b>Total</b>	<b>896</b>	<b>897</b>	<b>883</b>	<b>888</b>	<b>908</b>	<b>928</b>	<b>949</b>	<b>976</b>	<b>991</b>	<b>1,019</b>	<b>1,044</b>	<b>4,503</b>	<b>9,483</b>

(Continued)



**Table 3-5.****Continued**

(Billions of dollars)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Total, 2005- 2009	Total, 2005- 2014
<b>Discretionary Funding Is Frozen at the 2004 Level</b>													
Budget Authority													
Defense	460	464	464	464	464	464	464	464	464	464	464	2,318	4,636
Nondefense	416	420	418	418	418	420	418	417	417	417	417	2,094	4,181
<b>Total</b>	<b>876</b>	<b>884</b>	<b>881</b>	<b>882</b>	<b>881</b>	<b>883</b>	<b>881</b>	<b>881</b>	<b>881</b>	<b>881</b>	<b>881</b>	<b>4,412</b>	<b>8,816</b>
Outlays													
Defense	451	463	462	458	462	462	463	466	459	463	463	2,308	4,621
Nondefense	445	458	463	466	465	464	463	463	462	461	460	2,317	4,626
<b>Total</b>	<b>896</b>	<b>921</b>	<b>925</b>	<b>924</b>	<b>927</b>	<b>927</b>	<b>926</b>	<b>929</b>	<b>921</b>	<b>924</b>	<b>923</b>	<b>4,624</b>	<b>9,247</b>
<b>Memorandum:</b>													
Debt-Service Adjustment on Differences from CBO's Baseline													
Growth at 6.9 percent	*	*	3	7	15	26	40	58	80	107	139	51	475
Growth at nominal GDP	*	*	2	5	9	15	23	32	43	57	72	31	258
Excluding supplementals	*	-1	-3	-8	-13	-18	-24	-30	-37	-44	-51	-42	-227
Frozen at \$876 billion	*	*	-1	-3	-7	-11	-17	-25	-34	-45	-59	-23	-203

Source: Congressional Budget Office.

Notes: \* = between -\$500 million and \$500 million.

Discretionary funding comprises both budget authority and obligation limitations. Spending from the Highway Trust Fund and the Airport and Airway Trust Fund is subject to such limitations. Budget authority for those programs is provided in authorizing legislation and is not considered discretionary.

- Using the inflators specified in the Deficit Control Act (the GDP deflator and the employment cost index for wages and salaries).
- The 6.9 percent rate of growth is the historical average from 1999 through 2004, excluding \$87 billion in supplemental appropriations for 2004 enacted in November 2003. In this alternative, however, those supplemental appropriations are included in total budget authority for 2004 and are extended through 2014.

The second path assumes that the funding for 2004 grows at the average annual rate of nominal GDP after 2004 (4.6 percent a year, or nearly twice as fast as the rate of growth assumed in the baseline). Total discretionary outlays would exceed the baseline figures by almost \$1.4 trillion over the projection period under that scenario. Added debt-service costs would bring the cumulative increase in outlays to \$1.6 trillion.

The third path considers the impact on the baseline if the \$87 billion in supplemental appropriations for 2004 was not extended. Under that assumption, discretionary outlays over the 2005-2014 period would total about \$0.9 trillion less than in the baseline, with debt-service savings bringing the difference to \$1.1 trillion.

The final path shows less spending: it assumes that most discretionary budget authority (excluding certain rescissions of previous budget authority) and obligation limitations are frozen throughout the projection period at the level provided for 2004. Total discretionary outlays for the 10-year period would be \$1.1 trillion lower than those in the baseline scenario. Debt-service adjustments would reduce spending by another \$0.2 trillion.

## Entitlements and Other Mandatory Spending

More than half of the government's budget supports entitlement programs and other mandatory spending (excluding net interest payments). Most mandatory spend-

ing (also referred to as direct spending) reflects payments to individuals and other entities, such as businesses, non-profit institutions, and state and local governments. In general, those payments are governed by criteria set in law and are not normally constrained by the annual appropriation process. In addition, offsetting receipts (certain payments that government agencies receive from other agencies or from the public) are classified as offsets to mandatory spending.

Over the past 42 years, direct spending has grown significantly as a share of total federal outlays, climbing from 26 percent in 1962 to 55 percent in 2003. That upward trend is expected to continue, with such spending reaching nearly 59 percent of total outlays in 2014. Expressed as a percentage of GDP, mandatory outlays will increase from 10.9 percent currently to 11.8 percent by 2014 (including the effect of offsetting receipts), CBO projects. That trend primarily results from growth in outlays for the three largest programs—Social Security, Medicare, and Medicaid. Together, those three programs made up 71 percent of mandatory spending in 2003 (excluding payments of premiums that offset a portion of the costs of Medicare). That proportion is likely to continue to rise, reaching 80 percent by 2014, as more people are added to the ranks of beneficiaries and as increases in spending, fueled by cost-of-living adjustments, higher reimbursement rates, newly enacted laws (such as the recent Medicare bill), and other factors, compound throughout the coming decade.

Spending on mandatory programs is dominated by benefits for the nation's elderly. Social Security is by far the largest of all federal programs, paying benefits of nearly \$471 billion in 2003 (*see Table 3-6*). The number of people receiving benefits, already at more than 47 million, is expected to expand to 59 million by 2014, as more baby boomers (the large number of people born between 1946 and 1964) start to collect benefits in the coming years. Most Social Security beneficiaries also participate in Medicare, the program that pays for medical care for seniors and the severely disabled. Beginning in 2006, Medicare also will help defray the cost of their prescription drugs. Those two programs will continue to take up an increasing share of the federal budget. In 2003, combined outlays stood at nearly \$745 billion for Social Security and Medicare—over one-third of all federal government spending, or 6.9 percent of GDP. By 2014, spending for those two programs (excluding offsetting re-

ceipts) is projected to swell to 42 percent of all federal outlays, or 8.4 percent of GDP.

### Social Security

Benefit payments for Social Security are expected to climb at increasingly rapid rates throughout the next decade and beyond. The average growth rate for Social Security is projected to be 4.5 percent per year from 2004 through 2008 and to climb in the following years as baby boomers start to become eligible for benefits, reaching 6.3 percent by 2014. The overall growth rate of 5.3 percent for the 10-year period reflects different rates of growth for Social Security's main programs, Old-Age and Survivors Insurance, or OASI (5.2 percent), and Disability Insurance, or DI (6.3 percent).

Nearly \$400 billion in OASI benefits were paid in 2003 to more than 39 million people. The OASI program pays benefits to retired workers, their eligible spouses and children, and some survivors (primarily aged widows and young children) of deceased workers. Because about 60 percent of people ages 62 to 64, and more than 90 percent of people age 65 and over, collect OASI benefits, CBO ties its estimates of OASI beneficiaries chiefly to projections of the elderly population.

During the 1990s, spending on OASI benefits increased at an annual rate of 4.8 percent. That rate dropped to 3.3 percent in 2003, primarily because of low inflation, but it is expected to double—reaching 6.6 percent—by 2014. Although much of the projected growth is attributable to wage inflation and cost-of-living adjustments, growth in the number of people receiving OASI will become increasingly responsible for the rate of increase in OASI spending over the next 10 years, particularly once the leading edge of the baby-boom generation reaches retirement age.

The Social Security program also provides Disability Insurance benefits to qualified workers who have suffered a serious medical impairment before they reach retirement age, and to their eligible spouses and children. DI benefits totaled roughly \$70 billion in 2003—or about 15 percent of spending for all Social Security benefits. Payments for DI benefits are expected to grow at a faster clip this year (9.6 percent) than are benefits under OASI (3.8 percent in 2004). That rapid growth is projected to slow to 5.0 percent by 2014, the year in which the youngest of

**Table 3-6.****CBO's Baseline Projections of Mandatory Spending, Including Offsetting Receipts**

(Billions of dollars)													Total, 2005- 2009	Total, 2005- 2014
	Actual 2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014		
Social Security	471	492	513	533	559	587	618	653	690	732	778	827	2,809	6,490
Medicare <sup>a</sup>	274	294	317	369	418	448	478	515	557	592	645	698	2,029	5,035
Medicaid	161	174	179	186	195	212	230	250	271	295	320	348	1,003	2,487
Income-Support Programs														
Unemployment compensation	55	45	40	39	41	44	45	47	49	51	52	54	210	463
Supplemental Security Income	33	34	38	36	35	39	41	43	48	42	47	49	189	418
Earned income and child tax credits	38	40	44	41	41	40	40	41	44	31	31	32	207	386
Food Stamps	25	28	28	27	27	27	28	29	29	30	31	32	137	288
Family support <sup>b</sup>	26	26	25	25	25	25	25	25	26	26	26	27	126	256
Child nutrition	12	12	12	13	13	14	14	15	16	16	17	18	66	148
Foster care and adoption assistance	6	7	7	7	7	8	8	9	9	9	10	10	38	84
Subtotal	196	192	195	189	190	197	202	209	220	206	215	221	973	2,043
Other Retirement and Disability														
Federal civilian <sup>c</sup>	58	61	64	66	70	73	76	80	83	86	90	94	348	781
Military	36	38	39	40	41	43	44	46	47	48	49	50	208	448
Veterans' benefits <sup>d</sup>	29	32	37	35	33	36	36	36	40	35	38	39	176	365
Other	7	7	7	7	8	8	8	9	9	9	10	10	38	85
Subtotal	129	137	146	149	151	159	165	170	179	179	187	193	771	1,679
Other Programs														
Commodity Credit Corporation	15	12	14	15	15	14	15	15	15	15	14	14	74	146
TRICARE for Life	4	5	6	6	7	7	8	8	9	10	10	11	34	82
Student loans	8	4	6	6	7	7	7	7	7	7	8	8	33	70
Universal Service Fund	6	6	6	6	6	6	7	7	7	7	7	7	32	68
State Children's Health Insurance	4	5	5	5	5	5	5	5	5	6	6	6	25	53
Social services	5	5	5	5	5	5	5	5	5	5	5	5	24	49
Other	6	23	18	19	17	15	15	15	15	15	13	12	84	154
Subtotal	48	59	60	62	62	61	61	63	63	64	63	63	305	621
Offsetting Receipts	-100	-107	-115	-138	-151	-159	-163	-173	-184	-196	-208	-221	-726	-1,708
<b>Total</b>														
<b>Mandatory Spending</b>	<b>1,179</b>	<b>1,242</b>	<b>1,295</b>	<b>1,350</b>	<b>1,424</b>	<b>1,504</b>	<b>1,591</b>	<b>1,687</b>	<b>1,796</b>	<b>1,872</b>	<b>2,000</b>	<b>2,129</b>	<b>7,165</b>	<b>16,647</b>
<b>Memorandum:</b>														
Mandatory Spending Excluding														
Offsetting Receipts	1,279	1,349	1,409	1,489	1,575	1,664	1,754	1,860	1,980	2,067	2,208	2,349	7,891	18,355

Source: Congressional Budget Office.

Note: Spending for the benefit programs shown above generally excludes administrative costs, which are discretionary.

- a. Excludes offsetting receipts.
- b. Includes Temporary Assistance for Needy Families and various programs that involve payments to states for child support enforcement and family support, child care entitlements, and research to benefit children.
- c. Includes Civil Service, Foreign Service, Coast Guard, and other, smaller retirement programs and annuitants' health benefits.
- d. Includes veterans' compensation, pensions, and life insurance programs.

the baby boomers turns 50. Two factors account for much of the projected growth in Disability Insurance. First, the baby-boom generation is aging and more likely to have chronic disabilities. Second, the ongoing rise in Social Security's "normal retirement age" from 65 to 66—and eventually to 67—delays the reclassification of disabled workers as retired workers. As a result, older disabled individuals receive benefits under DI for a longer time before making the transition to OASI.

In addition to OASI and DI benefits, mandatory outlays for Social Security include about another \$4 billion a year, the bulk of which reflects an annual transfer to the Railroad Retirement program.

### Medicare

Spending for Medicare, the primary program that subsidizes medical benefits for the elderly, is expected to grow rapidly over the coming 10 years. The program currently is about 60 percent as large as Social Security, but by 2014, that proportion is projected to reach 84 percent. By that time, spending for Medicare (including mandatory administrative costs) will total \$698 billion, CBO projects, or almost 4 percent of GDP. The program's share of total federal spending will have increased to just over 19 percent from its 13 percent share in 2003.

Medicare currently comprises two main parts—Part A (Hospital Insurance) and Part B (Supplementary Medical Insurance). (Part C lays out the requirements for providers to participate in managed care plans, whose expenses are paid from the trust funds established for Parts A and B.) Under a new Part D of Medicare, beneficiaries will receive coverage for their prescription drugs. Medicare spending overall is estimated to rise by 7 percent in 2004 and by an average of 9 percent yearly through 2014. About half of the upswing in 2004 stems from automatic updates and legislated increases in payment rates for most services in the fee-for-service sector (including hospital care and services provided by physicians, home health agencies, and skilled nursing facilities). Those rates are subject to annual revisions based on changes in input prices as well as in economic factors such as GDP and productivity. Growth in the number of beneficiaries also will account for an increasing share of the rising costs for Medicare—as it will for Social Security—particularly as more baby boomers reach the age at which they qualify for benefits.

Beginning in 2006, a substantial rise in Medicare spending will come from the new prescription drug benefit. Ex-

penses for other provisions in the recently passed Medicare law (the Medicare Prescription Drug, Improvement, and Modernization Act of 2003, Public Law 108-173) will be incurred immediately, including increases in payments to health care providers and Medicare+Choice plans and administrative expenses associated with implementing the drug benefit.

Medicare's prescription drug program will subsidize coverage furnished in any of a number of ways: through a private prescription drug plan available to all Medicare enrollees in a geographic region; through a managed care plan participating in the Medicare Advantage program; or through an employer- or union-sponsored plan. Plans will charge beneficiaries premiums to pay for covered benefits not subsidized by Medicare. The program will provide additional federal subsidies to cover the costs of drugs for certain low-income Medicare beneficiaries. Spending for the drug program is expected to begin at \$47 billion (not including offsets from premium payments) in 2006, the first year in which the program is implemented, climbing to \$153 billion in 2014. By that time, expenditures under Part D will make up 22 percent of all Medicare spending. (*See Box 1-2 in Chapter 1 for a fuller discussion of how the new Medicare law will affect mandatory spending.*)

The growth of Medicare spending would be even more rapid were it not for the formula used to establish the fee schedule for physicians' services—the sustainable growth rate (SGR) formula. That formula sets a cumulative spending target for physicians' services and services related to physician visits (such as laboratory services and physician-administered drugs). Left unaltered, the SGR formula ultimately recoups spending above the cumulative target by reducing payment rates for physicians' services or by holding increases below inflation (as measured by the Medicare economic index). If spending falls short of the cumulative target, the SGR formula will provide for increases in payment rates above inflation.

By the end of 2002, spending subject to the SGR formula had exceeded the cumulative target by about \$17 billion, CBO estimated, and the amount of spending in excess of the target would have grown by another \$10 billion in the next few years. As a result, payment rates for 2003 were scheduled to drop by 4.4 percent (after a reduction of 5.4 percent in 2002). In the Consolidated Appropriations Resolution for 2003 (P.L. 108-7), the Congress responded to that imminent reduction by allowing the Administration to boost the cumulative target—thereby

producing a 1.6 percent increase in payment rates for physicians' services for 2003. But spending through 2003 exceeded that higher target by at least \$5 billion, CBO estimates. Therefore, the SGR formula would have again reduced payment rates, this time in 2004. However, P.L. 108-173 replaced that scheduled reduction in payment rates with increases of 1.5 percent in both 2004 and 2005—but left the cumulative target intact. Thus, spending for physicians' services will continue to exceed the cumulative target. Unless it is modified again, the SGR formula will reduce payment rates for several years beginning in 2006, and it will keep updates below inflation through at least 2014.

### Medicaid

Federal outlays for Medicaid, the joint federal/state program that pays for the medical care of many of the nation's poor, totaled \$161 billion in 2003, making up about 13 percent of mandatory spending (not including offsetting receipts). After growing by 14 percent in 2002, Medicaid outlays rose by 9 percent in 2003, marking the first decline in the program's growth rate in seven years. Growth slowed in 2003 because of smaller increases in enrollment and payment rates, cuts in payments to hospitals that serve a disproportionate share of Medicaid beneficiaries or other low-income people, and restrictions on financing mechanisms that states have used to generate additional federal payments. The drop in spending growth would have been even steeper if not for provisions in the Jobs and Growth Tax Relief Reconciliation Act of 2003 that increased federal matching rates for Medicaid for the last two quarters of 2003, thereby boosting outlays by an estimated \$4 billion.

CBO expects that spending for the program will rise by more than 8 percent in 2004, in part because of the increased federal matching rates, which will expire on June 30, 2004. Once those rates expire, spending growth is projected to fall back to roughly 3 percent in 2005. CBO anticipates that spending growth will remain low in 2006 and 2007 because the new Medicare drug benefit will relieve Medicaid of having to provide drug benefits to individuals who are eligible for both programs.

Despite those temporary declines, growth in Medicaid spending for later years is projected to remain robust because of rising prices, greater consumption of services, and, to a lesser extent, increased enrollment. After 2007, spending will increase by an average of nearly 9 percent annually, CBO projects, rising to \$348 billion in 2014.

As a result, by 2014, the federal government's Medicaid outlays are projected to reach 1.9 percent of GDP, compared with 1.5 percent in 2003.

### Other Income-Support Programs

In addition to Social Security, other federal programs provide cash assistance and other income support to people in need—those who cannot find work or whose income and assets fall below certain levels and who meet other criteria set in law. The programs include unemployment compensation, Supplemental Security Income, certain tax credits, and Food Stamps. When compared with the rapid increases in outlays projected for Social Security, Medicare, and Medicaid, spending for other income-support programs will inch upward at an average rate of about 3 percent over the next 10 years, CBO projects. The growth rate varies from year to year, largely because of economic fluctuations, legislated changes in some programs' parameters, and other factors, such as the number of payments in a fiscal year. (Payments for certain programs usually made on the first day of each month are made in the preceding month when that day falls on a holiday or weekend.)

CBO projects that as the pace of economic growth improves, and legislation to temporarily extend benefits for the unemployed expires, outlays for unemployment compensation will start to wane after three years of rapid growth. Spending on unemployment compensation will continue to fall through 2006, CBO estimates, mirroring the expected decline in the unemployment rate over the next few years—dropping from \$55 billion in 2003 to \$45 billion this year and to \$39 billion by 2006. Spending is projected to rise gradually thereafter as a result of increases in benefits and growth in the labor force.

Outlays for the Supplemental Security Income program, which provides cash benefits to low-income disabled children, adults, and the elderly, reached \$33 billion in 2003. SSI spending is projected to increase at a rate of just under 4 percent annually. The program's growth is driven mainly by cost-of-living-based increases in benefits and a rising caseload.

In CBO's baseline, estimates for the earned income and child tax credits reflect the scheduled increase in the amounts of such credits, and—in later years—the expiration of provisions in EGTRRA and JGTRRA. Together, the earned income and child tax credits totaled more than \$42 billion in 2003. In that year, a small portion of the credits showed up on the revenue side of the budget (as

lower taxes paid), but the majority (\$38 billion) was refunded to taxpayers and was reflected on the outlay side of the budget. Annual growth rates for the outlays of those tax credits are somewhat higher in the near term; JGTRRA increased the child tax credit from \$700 to \$1,000 per child for tax years 2003 and 2004, which will affect outlays in fiscal years 2004 and 2005. In tax year 2005, the credit falls to \$700 per child, resulting in a drop in outlays in fiscal year 2006. The credit then reverses course again—to \$800 in 2009 and to \$1,000 in 2010—resulting in increases in outlays for fiscal years 2010 and 2011. The steep dropoff in 2012 stems from the scheduled expiration of EGTRRA at the end of calendar year 2010, at which time the child tax credit will be refundable on a more limited basis and will be available only to families with three or more children.

In 2004, outlays for the Food Stamp program are anticipated to rise by 10 percent, to \$28 billion, following a 15 percent hike in 2003. (Between 1999 and 2001, before the recent economic slowdown, spending on Food Stamps was much lower, hovering between \$18 billion and \$19 billion a year.) CBO expects that participation in the Food Stamp program will follow its historical pattern (declines in program participation lag behind economic recovery) and will continue to rise over the next year before falling.

Although the authorization for Temporary Assistance for Needy Families (TANF) would have expired at the end of 2002, it was extended at various stages throughout 2003 and now is authorized through March 31, 2004. As required by the Deficit Control Act, CBO assumes that funding for TANF will continue at its most recently authorized level, an annual rate of \$17 billion. Spending under TANF, therefore, is projected to remain fairly stable throughout the coming decade. Including TANF, child support enforcement, and other child care entitlements, spending for family support services is estimated to total \$26 billion in 2004 and remain at about that level for the next 10 years.

In contrast, spending for child nutrition and for foster care and adoption assistance is projected to rise by about 4 percent a year through 2014. In 2003, outlays for child nutrition programs were \$12 billion, while spending for foster care and adoption assistance totaled \$6 billion.

### Other Federal Retirement and Disability Programs

In 2003, other federal retirement and disability programs incurred outlays of \$129 billion. Spending for those pro-

grams is projected to grow at about 4 percent per year and to remain at roughly 1 percent of GDP from 2003 through 2014.

The federal government provides benefits to its civilian and military retirees. In 2003, it provided nearly \$58 billion in annuities and survivors' benefits through its civilian retirement program, along with several smaller retirement programs. Those payments are expected to grow to almost \$94 billion by 2014. The increase is fueled by growth in the number of beneficiaries, cost-of-living adjustments, and rising federal salaries (which boost future benefit levels). One factor that is restraining growth somewhat is the gradual replacement of the Civil Service Retirement System (CSRS) with the less generous defined benefit under the Federal Employees Retirement System (FERS).<sup>4</sup>

Benefits paid to retired military personnel reached \$36 billion in 2003, and they are projected to rise to \$50 billion by 2014—an increase of about 3 percent per year. Recent enactment of legislation that permits certain disabled military retirees (and retirees of other uniformed services) to receive retirement annuities as well as veterans' disability benefits (referred to as concurrent receipt) will contribute to the rise in outlays.<sup>5</sup>

Spending for income-security-related benefits for veterans, which totaled \$29 billion in 2003, is projected to climb to \$39 billion in 2014, mainly because of cost-of-living adjustments and caseload increases.

### Other Mandatory Spending

After an initial increase of \$11 billion in 2004, other mandatory spending is expected to hover between \$59 billion and \$64 billion a year through 2014. Spending for farm price and income supports administered through the Commodity Credit Corporation will be fairly stable through 2014, CBO projects, ranging from \$12 billion to \$15 billion annually. In contrast, outlays for the TRICARE for Life program are expected to grow rapidly

4. Beginning in 1984, all newly hired federal civilian employees were enrolled in the FERS program. Although benefits under FERS by itself are less generous than benefits under CSRS, people enrolled in FERS are covered by Social Security and have contributions to the Thrift Savings Plan matched in part by their employers.

5. The National Defense Authorization Act for 2004 (P.L. 108-136) will allow concurrent receipt with no offset beginning on January 1, 2014. Those retirees will begin to receive an increasing portion of their retirement annuities over the 2004-2013 period.

(similar to the rate of growth of other medical expenditures), rising from \$5 billion in 2004 to \$11 billion by 2014. That program provides health care benefits to retirees of the uniformed services (and their dependents and surviving spouses) who are eligible for Medicare. For the student loan program, CBO estimates that the subsidy and administrative costs will range from \$4 billion to \$8 billion a year over the next decade.<sup>6</sup>

### What Drives the Growth in Mandatory Spending?

Over the past 25 years, mandatory spending has grown at a rapid clip. Growing at a rate of 7.2 percent per year, on average, mandatory spending outpaced nominal growth in the economy as well as inflation. CBO expects that trend to continue far into the future (under current law), with growth in mandatory spending (excluding offsetting receipts) averaging 5.7 percent a year from 2004 through 2014, largely as a result of demographic factors, cost-of-living adjustments, and rising health care costs. The bulk of federal spending supports benefits for the nation's elderly, so as larger portions of the population—particularly the baby-boom generation—reach retirement age, the swelling caseloads will put additional burdens on budgetary resources. Automatic increases in benefit amounts and other factors also will contribute significantly to the projected increases in mandatory spending.

The growing ranks of beneficiaries account for just over one-fourth of the projected growth in mandatory spending over the 2005-2014 period, increasing spending by \$19 billion in 2005 and by \$263 billion in 2014 relative to outlays in 2004 (*see Table 3-7*). The majority of that increase—about 79 percent—is concentrated in Social Security and Medicare, the two main programs that will be most affected by the growing number of elderly and disabled people. Programs that provide more benefits when the economy falters (such as unemployment compensation and Food Stamps) are expected to have fewer beneficiaries in coming years, as the economic recovery

continues. The dampening effect of such savings is modest, however.

The combined effect of automatic increases in benefits, along with cost-of-living and other adjustments, accounts for about 28 percent of the projected growth in mandatory spending. All of the major retirement programs grant automatic cost-of-living adjustments to their beneficiaries (the adjustment for 2004 is 2.1 percent). CBO estimates that those adjustments, which are pegged to the consumer price index, will be 1.5 percent in 2005, 1.8 percent in 2006, 2.1 percent in 2007, and 2.2 percent thereafter. As a result, cost-of-living adjustments are projected to add \$8 billion to total outlays in 2005 and \$144 billion in 2014 (accounting for about 14 percent of the growth estimated for the 10-year period).

Several other programs are indexed automatically to changes in prices and other economic factors. Adjustments to Medicare's payments to providers account for more than three-fourths of that type of growth. Those payments are based in part on price indexes for the medical sector and other economic factors, including changes in GDP and productivity. Adjustments to the earned income tax credit and the Food Stamp program also are automatically indexed. (Both the income thresholds above which the earned income tax credit begins to be phased out and the maximum amount of the tax credit are adjusted automatically for inflation using the consumer price index.)<sup>7</sup> The Food Stamp program adjusts its maximum benefit each year according to changes in the Department of Agriculture's Thrifty Food Plan (an adjusted estimate of minimum monthly food costs). The combined effect of indexing for all of those programs is an additional \$11 billion in outlays in 2005 and \$138 billion more in 2014, accounting for about 14 percent of mandatory spending growth.

The remaining 45 percent of growth in entitlement spending comes from increases that are not attributable to rising enrollment or automatic adjustments to benefit amounts. Other increases in Medicare and Medicaid, the establishment of Medicare Part D, and additional growth in Social Security contribute significantly to the projected increase in mandatory spending.

6. The costs for student loans that are included in the federal budget reflect only a small portion of the \$670 billion in loans expected to be made or guaranteed over the 10-year projection period. Under the Credit Reform Act, only the subsidy costs of the loans are treated as outlays. Those outlays are estimated as the future costs in today's dollars for interest subsidies, default costs, and other expected expenses over the life of the loans.

7. Credits for the EITC are administered through the individual income tax. Credits in excess of tax liabilities are recorded as outlays in the federal budget.

**Table 3-7.****Sources of Growth in Mandatory Spending**

(Billions of dollars)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Estimated Spending for Base Year 2004	1,349	1,349	1,349	1,349	1,349	1,349	1,349	1,349	1,349	1,349
Sources of Growth										
Increases in caseloads	19	31	53	77	101	127	154	188	225	263
Automatic increases in benefits										
Cost-of-living adjustments	8	20	33	48	63	79	95	110	127	144
Other <sup>a</sup>	11	19	29	40	54	69	85	102	120	138
Other increases in Medicare and Medicaid <sup>b</sup>	6	22	39	56	77	101	126	151	178	209
Establishment of Medicare prescription drug benefit <sup>c</sup>	1	40	60	68	74	81	89	98	110	123
Other growth in Social Security <sup>d</sup>	7	11	18	25	34	45	58	74	92	113
Irregular number of benefit payments <sup>e</sup>	9	-3	-6	*	*	*	11	-11	*	*
Other sources of growth	*	*	*	*	1	8	13	6	8	10
<b>Total</b>	<b>61</b>	<b>140</b>	<b>226</b>	<b>315</b>	<b>405</b>	<b>511</b>	<b>631</b>	<b>718</b>	<b>859</b>	<b>1,000</b>
Projected Spending	1,409	1,489	1,575	1,664	1,754	1,860	1,980	2,067	2,208	2,349

Source: Congressional Budget Office.

Note: \* = between zero and \$500 million.

- Includes automatic increases in the Food Stamp program and child nutrition benefits, certain Medicare reimbursement rates, the earned income tax credit, and other programs.
- All growth that is not attributed to increased caseloads, automatic increases in reimbursement rates, or new legislation. Excludes most of the new Medicare drug benefit but includes the provider provisions. Excludes offsetting receipts.
- Excludes premium collections and other offsetting receipts, as well as the effects of legislation that relate to other provisions affecting provider payments.
- All growth that is not attributed to increased caseloads and cost-of-living adjustments.
- Represents differences attributable to the number of benefit checks that will be issued in a fiscal year. Normally, benefit payments are made once a month. However, Medicare will make 13 payments of benefits in 2005 and 2011 and 11 payments in 2006 and 2012. Supplemental Security Income and veterans' benefits will be paid 13 times in 2005 and 2011 and 11 times in 2007 and 2012.

CBO anticipates that rising inflation will contribute to increased spending for Medicaid, even though the program is not formally indexed at the federal level. Medicaid payments to providers are determined at the state level, and the federal government matches those payments according to a formula set by law. If states increase their benefits in response to higher prices, federal payments will rise in tandem. In addition, Medicare, Medicaid, and other health programs have faced steadily escalating costs, as participants consume more health services per capita and increasingly use more costly procedures. CBO estimates that growth from those sources will contribute \$6 billion more to outlays in 2005 and \$209 billion more in 2014.

The new Medicare law will be responsible for about 15 percent of the projected growth in mandatory spending. P.L. 108-173 will add about \$1 billion to outlays in 2005, rising to \$123 billion by 2014.<sup>8</sup>

The growth of average benefits for Social Security recipients and most federal retirees is faster than the increase provided by cost-of-living adjustments alone. In the case of Social Security, the initial amount available to a newly eligible individual depends on his or her age and past earnings; only after that benefit is set do COLAs adjust it

8. Those amounts do not include premiums and other offsetting receipts, which, if included, would result in a net increase of \$81 billion by 2014 compared with the spending level in 2004.



in step with changes in the consumer price index. Because awards to new beneficiaries are indexed to growth in wages, and wage growth typically exceeds inflation, their benefits generally are higher than the monthly check of a longtime beneficiary who has been receiving only cost-of-living adjustments since retiring. Furthermore, because women's participation in the labor force grew dramatically beginning in the mid-1960s, more new retirees receive larger benefits based on their own earnings rather than smaller benefits based on their status as a spouse of a retiree. For Social Security, CBO estimates that the resulting increases in benefits will add \$113 billion, or 11 percent, to outlays in 2014. Only one-fourth of that increase depends on the wage growth that CBO projects over the 2004-2014 period; the rest reflects wage growth that has already occurred over the past three decades.

Outlays for mandatory programs also depend on whether the first day of the fiscal year, October 1, falls on a weekday or weekend. If it falls on a weekend, some benefit payments will be made at the end of September, a shift that increases spending in the preceding year and decreases spending for the coming year. Because SSI, veterans' compensation and pension programs, and Medicare payments to health maintenance organizations are affected by such timing shifts, those programs may send out 11, 12, or 13 monthly checks in a fiscal year. (For example, Medicare, SSI, and veterans' benefits will be paid 13 times in 2005.) Irregular numbers of benefit payments will affect mandatory spending in 2005, 2006, 2007, 2011, and 2012.

The remaining growth in mandatory spending comes from a number of factors: rising benefits for new retirees in the civil service and military retirement programs (reflecting the same economic phenomenon as in Social Security); larger average benefits for unemployment compensation (a program that lacks a specific COLA but which pays benefit amounts that generally are linked to the recent earnings of its beneficiaries); and other sources. Offsetting some of those factors is the expiration of emergency benefits for unemployment insurance. The scheduled expiration of EGTRRA at the end of calendar year 2010 also will help hold down growth in this area by returning the earned income and child tax credits to their pre-2002 levels.

### Offsetting Receipts

Offsetting receipts are payments from the public or intragovernmental transactions that the federal government records as negative spending—that is, offsets to mandatory spending. Examples of those receipts include payments of premiums for Medicare and agencies' contributions to retirement funds. The collection of offsetting receipts will reduce total mandatory spending by between 8 percent and 10 percent each year through 2014, CBO projects.

**Medicare.** Over the 10-year projection period, the largest component of offsetting receipts will consist of premiums and other receipts of the Medicare program. In 2003, payments of premiums under Parts A and B of Medicare totaled \$28 billion and offset about 10 percent of that program's spending (*see Table 3-8*). By 2014, with the addition of premiums under Part D and other payments from states' Medicaid programs, Medicare premiums and other receipts are projected to reach \$114 billion. At that time, they will finance about 16 percent of the program's costs.

Most of the beneficiaries under Part A of Medicare, the Hospital Insurance program, are not charged a premium. However, Medicare collects premiums for about 400,000 enrollees who were not employed in jobs covered by Medicare payroll taxes long enough to qualify for free enrollment. Medicaid pays the Part A premium for most of those beneficiaries. Those payments, which totaled \$2 billion in 2003, are estimated to rise modestly to \$3 billion by 2014.

The majority of Medicare premiums are paid by the 39 million people enrolled in Supplementary Medical Insurance (Part B of Medicare), which primarily covers physicians' and outpatient hospital services. By law, those premiums are set to cover one-quarter of the program's costs. The average monthly charge for beneficiaries is \$67 in 2004; it is expected to grow to \$114 in 2014. (Medicaid pays the Part B premium for certain low-income enrollees.) In addition, the recently enacted Medicare law establishes higher premiums, beginning in 2007, for beneficiaries with relatively high incomes. In 2014, about 6 percent of beneficiaries will be subject to those elevated premiums, CBO estimates, which will be as high as \$365 a month. Total Part B premiums are projected to rise from \$30 billion in 2004 to \$70 billion in 2014.

CBO estimates that the introduction of the premiums for Part D of Medicare will lead total premiums collected

**Table 3-8.****CBO's Baseline Projections of Offsetting Receipts**

(Billions of dollars)

	Actual 2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Total, 2005- 2009	Total, 2005- 2014
Medicare <sup>a</sup>	-28	-32	-36	-54	-63	-68	-74	-81	-88	-96	-105	-114	-295	-779
Employer's Share of Employee Retirement														
Social Security	-10	-11	-11	-12	-13	-14	-15	-16	-17	-17	-18	-19	-65	-152
Military retirement	-14	-14	-13	-13	-13	-14	-14	-15	-15	-16	-16	-16	-68	-145
Civil service retirement and other	-18	-19	-20	-21	-21	-22	-23	-24	-25	-26	-27	-28	-108	-236
Subtotal	-41	-44	-45	-46	-48	-50	-52	-54	-57	-59	-61	-62	-240	-533
TRICARE for Life	-8	-9	-12	-13	-13	-14	-15	-16	-17	-18	-19	-20	-67	-157
Energy-Related Receipts <sup>b</sup>	-6	-6	-6	-7	-7	-8	-7	-7	-7	-7	-8	-8	-36	-73
Natural Resources-Related Receipts <sup>c</sup>	-4	-4	-4	-4	-4	-4	-4	-4	-4	-4	-4	-4	-18	-37
Electromagnetic Spectrum Auctions	*	*	*	-5	-5	-5	*	*	*	*	*	*	-15	-15
Other <sup>d</sup>	-12	-12	-12	-10	-11	-11	-11	-11	-11	-12	-12	-12	-54	-112
<b>Total</b>	<b>-100</b>	<b>-107</b>	<b>-115</b>	<b>-138</b>	<b>-151</b>	<b>-159</b>	<b>-163</b>	<b>-173</b>	<b>-184</b>	<b>-196</b>	<b>-208</b>	<b>-221</b>	<b>-726</b>	<b>-1,708</b>

Source: Congressional Budget Office.

Note: \* = between -\$500 million and zero.

- a. Includes Medicare premiums and amounts withheld from payments to states' Medicaid programs and transferred to the Part D account in the Supplementary Medical Insurance Trust Fund.
- b. Includes proceeds from the sale of electricity, various fees, and Outer Continental Shelf receipts.
- c. Includes timber and mineral receipts and various fees.
- d. Includes asset sales.

under Medicare to increase by 33 percent in 2006, the first year in which the new benefit will be available. Participants in the drug benefit will pay a premium, expected to average about \$35 per month in 2006, rising to \$58 per month in 2014. Those premiums will cover about one-sixth of the costs of the Part D program, CBO estimates. Those collections are expected to grow steadily—at about 9 percent each year—after the new program is under way, increasing from \$9 billion in 2006 to \$26 billion in 2014.

The introduction of Part D of Medicare will allow states to spend less on Medicaid benefits, CBO estimates, as the costs of subsidizing prescription drugs for low-income seniors shift from Medicaid (a program for which the states

and federal government share the costs) to Medicare. The Medicare legislation required the states to return a portion of those savings to the Treasury. Those funds would be credited to the Medicare Part B trust fund. CBO projects that those transfers will grow from \$6 billion in 2006 to \$16 billion in 2014.

**Other Offsetting Receipts.** Currently, the largest component of offsetting receipts is the intragovernmental transfers that federal agencies make to their employees' retirement plans. At \$44 billion in 2004, those contributions will constitute about 40 percent of total offsetting receipts in that year. That proportion will fall to about 30 percent by 2014, as rising payments for Medicare premiums take over as the main source of offsetting receipts.

Such intragovernmental transfers will continue to rise, totaling a projected \$62 billion in 2014. Agencies' contributions for retirement benefits are paid primarily to the trust funds for Social Security, military retirement, and civil service retirement. They are charged against the agencies' budgets in the same way that other elements of their employees' compensation are: the budget treats them as outlays of the employing agency and records the deposits in the retirement funds as offsetting receipts. The transfers net to zero in budgetary totals, leaving only the funds' disbursements—for retirement benefits and administrative costs—reflected as outlays.

As with their retirement plans, some defense and related agencies make intragovernmental transfers to the Uniformed Services Medicare-Eligible Retiree Health Care Fund under the TRICARE for Life program. That fund pays for certain health care expenses of retirees from the uniformed services, their dependents, and surviving spouses who are eligible for Medicare. Its total receipts are expected to more than double, rising from \$9 billion in 2004 to \$20 billion in 2014.

Auctions by the Federal Communications Commission of rights to use parts of the electromagnetic spectrum are expected to continue until that authority expires at the end of 2007. CBO estimates that those auctions will bring in about \$15 billion over the 2005-2014 period, with most of the receipts being tallied between 2006 and 2008.

Other proprietary receipts come mostly from royalties and charges for oil and natural gas production on federal lands, electricity sales from federal hydroelectric facilities, mineral and timber sales from federal lands, and various fees levied on users of public property and services. Those receipts are expected to total between \$10 billion and \$12 billion annually.

### Legislation Assumed in the Baseline

CBO's projections for mandatory spending follow the general baseline concept of estimating future budget authority and outlays in accordance with current law. However, in the case of certain mandatory programs with outlays of more than \$50 million in the current year, the Deficit Control Act directs CBO to assume that the programs will be extended when their authorization expires.<sup>9</sup>

The Food Stamp program, Temporary Assistance for Needy Families, agricultural assistance provided by the Commodity Credit Corporation, and the State Chil-

dren's Health Insurance Program are examples of programs whose current authorizations are set to expire but in the baseline are assumed to continue. The Deficit Control Act also directs CBO to assume that a cost-of-living adjustment for veterans' compensation is granted each year. The assumption that expiring programs will continue accounts for more than \$7 billion in outlays in 2004; that figure increases to nearly \$82 billion by 2014 (see Table 3-9).

### Net Interest

Interest costs in 2004 will total \$156 billion, CBO estimates, \$3 billion more than in 2003 (see Table 3-10 on page 68). If that estimate holds, it will mark the first time since 1997 that interest costs have grown from one year to the next. In 1997, net interest costs totaled \$244 billion, their record high in nominal dollar terms; over the following six years, however, interest outlays decreased as a result of budget surpluses and declining interest rates. CBO's baseline shows 11 consecutive years of increasing interest costs, in large part the result of accumulating debt as well as rising interest rates in CBO's economic forecast. In 2014, net interest costs will total \$338 billion, CBO projects, more than double their level in 2003.

The federal government's interest payments depend mostly on the amount of outstanding debt held by the public and on interest rates. The Congress and the President can influence the former through legislation governing taxes and spending and, thus, the amount of government borrowing. Interest rates are determined by market forces and the Federal Reserve's policies.

Interest costs are also affected by the composition of debt held by the public. The average maturity of outstanding marketable debt has remained fairly constant, fluctuating between roughly five years and six years since 1986, despite some changes in the types of securities issued by the Treasury Department. For example, in 2001, the Treasury stopped issuing 30-year bonds and introduced a four-week bill. As a result, the average maturity of outstanding debt has fallen from five and three-quarters

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9. Section 257 of the Deficit Control Act stipulates that programs with current-year outlays of \$50 million or more that were established prior to enactment of the Balanced Budget Act of 1997 are assumed in the baseline to continue but that the treatment of programs established after the 1997 law will be decided on a case-by-case basis, in consultation with the House and Senate Budget Committees.

**Table 3-9.****Costs for Mandatory Programs That CBO's Baseline Assumes Will Continue Beyond Their Current Expiration Dates**

(Billions of dollars)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Total, 2005- 2009	Total, 2005- 2014
Food Stamps													
Budget authority	n.a.	n.a.	n.a.	n.a.	27.4	28.0	28.7	29.4	30.1	30.9	31.7	55.4	206.2
Outlays	n.a.	n.a.	n.a.	n.a.	26.0	28.0	28.7	29.4	30.1	30.9	31.7	54.0	204.6
Temporary Assistance for Needy Families													
Budget authority	6.9	16.9	16.9	16.9	16.9	16.9	16.9	16.9	16.9	16.9	16.9	84.4	168.9
Outlays	6.2	16.4	17.6	17.4	17.0	16.9	16.9	16.9	16.9	16.9	16.9	85.3	169.7
Commodity Credit Corporation <sup>a</sup>													
Budget authority	n.a.	n.a.	n.a.	n.a.	n.a.	15.3	15.1	14.9	14.6	14.3	13.7	15.3	87.9
Outlays	n.a.	n.a.	n.a.	n.a.	n.a.	15.3	15.1	14.9	14.6	14.3	13.7	15.3	87.9
Veterans' Compensation COLAs													
Budget authority	n.a.	0.4	0.9	1.4	2.1	2.7	3.3	4.1	4.1	5.1	5.7	7.4	29.7
Outlays	n.a.	0.4	0.9	1.4	2.0	2.6	3.2	4.1	4.1	5.0	5.6	7.3	29.3
Child Care Entitlement to States													
Budget authority	0.8	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	13.6	27.2
Outlays	0.8	2.2	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	2.7	13.0	26.6
State Children's Health Insurance Program													
Budget authority	n.a.	n.a.	n.a.	n.a.	5.0	5.0	5.0	5.0	5.0	5.0	5.0	10.1	35.3
Outlays	n.a.	n.a.	n.a.	n.a.	1.6	4.3	5.1	5.4	5.5	5.6	5.5	5.9	33.0
Rehabilitation Services and Disability Research													
Budget authority	n.a.	n.a.	n.a.	2.7	2.8	2.9	2.9	3.0	3.0	3.1	3.2	8.4	23.6
Outlays	n.a.	n.a.	n.a.	1.1	2.2	2.8	2.9	2.9	3.0	3.1	3.1	6.1	21.1
Ground Transportation Programs Not Subject to Annual Obligation Limitations													
Budget authority	0.4	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6	3.2	6.4
Outlays	0.1	0.3	0.5	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6	2.6	5.8
Federal Unemployment Benefits and Allowances													
Budget authority	n.a.	n.a.	n.a.	n.a.	0.9	0.9	0.9	0.9	0.9	0.9	1.0	1.7	6.3
Outlays	n.a.	n.a.	n.a.	n.a.	0.4	0.8	0.9	0.9	0.9	0.9	0.9	1.2	5.7

(Continued)

**Table 3-9.****Continued**

(Billions of dollars)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Total, 2005- 2009	Total, 2005- 2014
Child Nutrition <sup>b</sup>													
Budget authority	0.4	0.4	0.4	0.4	0.4	0.5	0.5	0.5	0.5	0.5	0.5	2.1	4.6
Outlays	0.3	0.4	0.4	0.4	0.4	0.5	0.5	0.5	0.5	0.5	0.5	2.1	4.6
Family Preservation and Support													
Budget authority	n.a.	n.a.	n.a.	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.9	2.4
Outlays	n.a.	n.a.	n.a.	0.1	0.2	0.3	0.3	0.3	0.3	0.3	0.3	0.6	2.1
Health Resources and Services Administration													
Budget authority	0	0	0	0	0	0	0	0	0	0	0	0	0
Outlays	0	0	0	0	0	0	0	0	0	0	0	0	0
Ground Transportation Programs Controlled by Obligation Limitations <sup>c</sup>													
Budget authority	23.5	40.4	40.4	40.4	40.4	40.4	40.4	40.4	40.4	40.4	40.4	201.8	403.7
Outlays	0	0	0	0	0	0	0	0	0	0	0	0	0
Air Transportation Programs Controlled by Obligation Limitations <sup>c</sup>													
Budget authority	3.3	3.5	3.6	3.7	3.7	3.7	3.7	3.7	3.7	3.7	3.7	18.2	36.7
Outlays	0	-0.2	-0.1	*	0.2	0.1	0.1	*	*	*	*	*	*
<b>Total</b>													
Budget authority	35.4	64.9	65.6	69.2	103.2	119.8	121.0	122.5	123.0	124.5	125.4	422.6	1,038.9
Outlays	7.4	19.5	22.0	23.6	53.4	74.8	76.9	78.7	79.2	80.8	81.7	193.4	590.6

Source: Congressional Budget Office.

Note: \* = between zero and \$50 million; n.a. = not applicable; COLAs = cost-of-living adjustments.

- a. Agricultural commodity price and income supports under the Farm Security and Rural Investment Act of 2002 (FSRIA) generally expire after payments are made for the 2007 crop year. Much of that spending will occur in 2008. Although permanent price support authority under the Agricultural Adjustment Act of 1939 and the Agricultural Act of 1949 would then become effective, section 257(b)(2)(iii) of the Deficit Control Act says that the baseline must assume that the FSRIA provisions continue.
- b. Includes the Summer Food Service program and states' administrative expenses.
- c. Authorizing legislation provides contract authority, which is counted as mandatory budget authority. However, because spending is subject to obligation limitations specified in annual appropriation acts, outlays are considered discretionary.

**Table 3-10.****CBO's Baseline Projections of Federal Interest Outlays**

(Billions of dollars)

	Actual 2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Total, 2005- 2009	Total, 2005- 2014
Interest on Public Debt (Gross interest) <sup>a</sup>	318	321	351	407	460	504	542	578	611	640	664	690	2,264	5,447
Interest Received by Trust Funds														
Social Security	-84	-79	-90	-100	-111	-121	-132	-142	-153	-173	-183	-203	-554	-1,407
Other trust funds <sup>b</sup>	-73	-76	-70	-74	-78	-84	-90	-98	-106	-106	-117	-117	-396	-941
Subtotal	-156	-155	-160	-174	-189	-205	-222	-240	-259	-279	-300	-320	-950	-2,347
Other interest <sup>c</sup>	-7	-9	-11	-13	-15	-17	-19	-21	-24	-26	-28	-31	-75	-205
Other investment income <sup>d</sup>	-2	*	-1	-1	-1	-1	-1	-1	-1	-1	-1	-1	-4	-8
<b>Total (Net interest)</b>	<b>153</b>	<b>156</b>	<b>180</b>	<b>219</b>	<b>255</b>	<b>281</b>	<b>300</b>	<b>316</b>	<b>328</b>	<b>334</b>	<b>335</b>	<b>338</b>	<b>1,235</b>	<b>2,886</b>

Source: Congressional Budget Office

Note: \* = between -\$500 million and zero.

- a. Excludes interest costs of debt issued by agencies other than the Treasury (primarily the Tennessee Valley Authority).
- b. Mainly the Civil Service Retirement, Military Retirement, Medicare, and Unemployment Insurance Trust Funds.
- c. Primarily interest on loans to the public.
- d. Earnings on private investments by the National Railroad Retirement Investment Trust.

years in December 2000 to four and three-quarters years in September 2003. Currently, Treasury bills with a maturity of six months or less account for about 27 percent of all marketable debt (a similar proportion is assumed throughout the 10-year projection period); although such securities generally carry lower interest rates, they will be more sensitive than longer-term maturities to rapid changes in interest rates.

From 2004 to 2008, net interest costs are projected to climb from \$156 billion to \$281 billion—in large part because of the growth of more than \$1.2 trillion in debt held by the public to finance projected deficits and the return to higher short-term interest rates in CBO's economic forecast. By 2008, interest costs in the baseline will consume more than 10 percent of total outlays. As a share of GDP, they are projected to grow to 2.0 percent in 2008 from 1.4 percent in 2004. (By contrast, net interest as a share of the economy ranged between 2.1 percent of GDP and 3.3 percent each year between 1981 and 2001.)

After 2008, projected interest rates stabilize. As a result, the change in baseline net interest will mirror the change in debt held by the public, which continues growing in every year until 2014. Under current policies, CBO projects that net interest will represent 1.9 percent of GDP and 9.3 percent of total outlays by 2014.

The federal government has issued about \$2.9 trillion in securities to federal trust funds. Similar to the composition of debt held by the public, those securities consist of bills, notes, bonds, inflation-indexed securities, and zero-coupon bonds. However, unlike such debt, the interest from those securities has no budgetary impact, because it is credited to accounts that exist elsewhere in the budget. In 2004, trust funds will receive \$155 billion of interest, CBO estimates—the bulk of which will be credited to the Social Security and Civil Service Retirement Trust Funds.

The \$9 billion in other interest that CBO anticipates the government will receive in 2004 represents the net of certain interest payments and interest collections. On balance, the government earns more of such interest than it

pays out. Among its interest expenses are payments for interest on tax refunds that are delayed for more than 45 days after the filing date. On the collections side, the interest received from the financing accounts of credit programs, such as direct student loans, is among the larger categories. Although other interest appears to grow rapidly throughout the projection period, nearly all of that

increase is attributable to interest on the accrued balances credited to the TRICARE for Life program. (Interest payments to the program are part of interest on the public debt, and the receipts are recorded in the other-interest category; the net effect on interest outlays is zero.)

